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SUBJECT: LOAN DEFAULTS RISE WITH INCREASE IN CONSUMER CREDIT

REF: BOGOTA 583

11. SUMMARY: After five years of strong economic growth, consumer credit has reached record levels in Colombia. However, the rise in consumer lending has also led to an increase in loan defaults and suggestions that such defaults could harm the solvency of Colombia's booming financial sector (reftel). Despite the higher number of overextended Colombian consumers, most financial observers downplay the risk to the banking industry and emphasize that the number of defaulted loans remains low as a percentage of total lending and is centralized within specialized lending institutions. END SUMMARY.

Just Charge It

12. Consumer lending increased 32 percent in 2007 after growing 35 percent in 2006. During the same period loan defaults increased 55 percent. While the total percentage of consumer loans that result in default remained relatively low at 3.25 percent, the steep percentage increase in consumer credit and defaults has led some Central Bank officials to worry that local financial institutions are lowering their lending standards to aggressively pursue the lucrative consumer loan market.

Financial Sector Largely Insulated

13. Nevertheless, local financial experts tell us that the private banking sector remains generally insulated from the threat of portfolio erosion since most of the defaults center in government-owned specialized lending institutions such as the Public Education Credit Fund (ICETEX). Carlos Rojas, Vice President of the Association of Financial Institutions (ANIF), expressed doubt that the overall financial sector would experience any destabilization at the current rate of defaults. He emphasized that the banking sector possesses strong capital reserves and enjoys well-diversified lending portfolios, including strong positions in the stable commercial lending market.

Still, Maybe Time to Rein It In

14. Colombian Banking Association (Asobancaria) President Maria Mercedes Cuellar echoed the view that the banking sector maintains a very diversified credit portfolio and faces minimal threat from the increase in consumer lending defaults. She characterized the increase in consumer credit

as a positive indicator of Colombia's economic development and a legitimate extension of the financial sector to a market segment that has long been underserved. However, Cuellar suggested that Colombia's financial system would benefit from closer examination of consumer credit patterns and incorporation of that data into updated loan quality and risk management models in order to avoid developing a consumer credit bubble.

Brownfield